



Financial Management Report as of June 30, 2011

AT A GLANCE:

County and City Officials Applaud Transition of North Juanita, Finn Hill & Kingsgate (page 2 sidebar)

2011 revenues are ahead of 2010 year-to-date due to annexation tax assumptions, accounting changes, and some improvements in other categories (page 3)

2011 Sales tax revenue ahead of 2010 (page 5)

Economy weakened further in June (pages 7-8)

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The Financial Management Report will be a challenge to interpret in 2011 due to annexation, which will impact expenditures and revenues at different times throughout the year. In particular, the City incurred increasing expenses month-by-month to gear up for annexation, but no revenue from the annexation area was collected until July and the bulk of the revenue will not be received until the fourth quarter. To accommodate this dynamic, some revenue sources, such as property tax, were allocated differently in 2011 than in 2010, as highlighted below. As a result, this quarter's FMR will be the last to discuss the comparison of 2011 actual results to last year; instead, the analysis in the next several reports will compare the 2011 actual results to the 2011 budget.

Summary of All Operating Funds: *Revenue*

- **General Fund** actual 2011 revenue is **19.9 percent ahead** of the same period last year (more than \$5 million). Several factors contribute to this increase, including the reallocation of property tax from the Street Fund to the General Fund in recognition that the City will receive a large payment of the County's road tax in the Street Fund at the end of 2011. Other factors include the receipt of two-thirds of the second quarter Fire District 41 payment in May (the second quarter payment was received during the third quarter in 2010) and the impact of combining the Recreation Revolving Fund with the General Fund in 2011 to recognize accounting changes required by recent revision to accounting standards. A more detailed analysis of General Fund revenue can be found on page 3, and sales tax revenue performance can be found beginning on page 5.
- **Other General Government Funds** actual 2011 revenue is down **17.2 percent** compared to the same period last year, in part due to two of the factors described above:
- **Water Sewer Operating Fund** actual 2011 revenue is **4.1 percent ahead** of the same period last year, largely due to a sewer rate increase.
- **Surface Water Management Fund** actual 2011 revenue is **5.7 percent ahead** of the same period last year. Rate revenue is up 5.8 percent, partially due to a rate increase effective in 2011. Rates are paid through property taxes, which are primarily received in April and October.
- **Solid Waste Fund** actual 2011 revenue is **0.4 percent behind** the same period last year.

Resources by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2010	6/30/2011	% Change	2010	2011	% Change	2010	2011
General Gov't Operating:								
General Fund	26,145,298	31,338,863	19.9%	54,706,544	69,725,756	27.5%	47.8%	44.9%
Other General Gov't Operating Funds	8,057,531	6,674,448	-17.2%	15,798,095	16,490,820	4.4%	51.0%	40.5%
Total General Gov't Operating	34,202,829	38,013,311	11.1%	70,504,639	86,216,576	22.3%	48.5%	44.1%
Utilities:								
Water/Sewer Operating Fund	8,523,400	8,872,474	4.1%	20,660,066	19,810,646	-4.1%	41.3%	44.8%
Surface Water Management Fund	2,759,468	2,917,577	5.7%	5,270,500	6,477,992	22.9%	52.4%	45.0%
Solid Waste Fund	4,140,088	4,124,632	-0.4%	8,627,630	12,810,339	48.5%	48.0%	32.2%
Total Utilities	15,422,956	15,914,683	3.2%	34,558,196	39,098,977	13.1%	44.6%	40.7%
Total All Operating Funds	49,625,785	53,927,994	8.7%	105,062,835	125,315,553	19.3%	47.2%	43.0%

Budgeted and actual revenues exclude resources forward and interfund transfers.



County and City Officials Applaud Transition of North Juanita, Finn Hill & Kingsgate

King County Executive Dow Constantine joined with Kirkland City leaders and King County Councilmember's to mark the largest shift of unincorporated county territory in recent memory – the annexation by the City of Kirkland of nearly seven square miles of the North Juanita, Finn Hill and Kingsgate areas.

The annexation took effect at 12:01 a.m. on June 1, 2011, and brought more than 31,000 residents to the City of Kirkland.

"We welcome our new residents and look forward to providing our services that reflect our commitment to quality of life," notes Kirkland Mayor Joan McBride. "It's taken a lot of focused effort between the City and the County to make this annexation become a reality. We appreciate the tremendous support we have received from King County to make this transition possible. We are also extremely proud of our City employees and their dedication in preparing to serve our new residents in this area. We are excited to join as one City, one Kirkland."

In November 2009, the question of annexation, zoning regulations, and assumption of indebtedness was placed on the ballot for voters in the annexation area. A strong majority of more than 59 percent approved annexation to Kirkland, but a companion measure regarding the assumption of indebtedness did not receive the required 60 percent voter approval. The Kirkland City Council accepted the annexation in December 2009 without imposing the assumption of the City's previous voter-approved indebtedness.

To learn more about the City of Kirkland, visit www.kirklandwa.gov.

Summary of All Operating Funds: *Expenditures*

- **General Fund** actual expenditures are **7.1 percent ahead** of last year primarily due to increased personnel and supply costs associated with preparation for annexation, public safety radio replacement and the restoration of a 3.4 percent salary reduction taken by most employees related to furlough days in 2010. A more detailed analysis of General Fund expenditures by department is found on page 4.
- **Other Operating Funds** actual expenditures are **8.9 percent ahead** of the same period last year due to higher computer hardware expenses, substantially higher facility utility costs, an increase in vehicle/equipment purchases and an increase in replacement and operating and maintenance costs for vehicles and equipment. Facility utility costs are up more than 50 percent, mainly due to changes in weather patterns and partially due to the addition of the building purchased for the public safety facility. Vehicle and computer hardware costs vary year-to-year depending on the planned replacement cycle, 2011 will continue to see a significant increase in cost over 2010 due to annexation.
- **Water/Sewer Operating Fund** actual expenditures are **14.9 percent ahead** of the same period last year primarily due to an increase in sewer charges and an increase in water purchases. This comparison is skewed by the fact that regional water connection charges were significantly lower in the first half of 2010 compared to 2011.
- **Surface Water Management Fund** actual expenditures are **0.6 percent behind** the same period last year due to lower personnel costs and normal variability in the timing of payment for various services.
- **Solid Waste Fund** actual expenditures are **27.0 percent behind** the same period last year due to the timing of disposal contract billing payments, in this case the May and June 2011 payments were not invoiced and posted until July 2011. The individual monthly contract payments are significant, so timing of the payments can skew comparisons.

Expenditures by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2010	6/30/2011	% Change	2010	2011	% Change	2010	2011
General Gov't Operating:								
General Fund	28,234,263	30,245,797	7.1%	58,149,798	67,468,176	16.0%	48.6%	44.8%
Other General Gov't Operating Funds	6,231,570	6,787,369	8.9%	13,326,213	16,606,912	24.6%	46.8%	40.9%
Total General Gov't Operating	34,465,833	37,033,166	7.4%	71,476,011	84,075,088	17.6%	48.2%	44.0%
Utilities:								
Water/Sewer Operating Fund	7,107,489	8,168,238	14.9%	15,903,927	16,454,624	3.5%	44.7%	49.6%
Surface Water Management Fund	1,630,678	1,620,246	-0.6%	3,387,458	4,338,993	28.1%	48.1%	37.3%
Solid Waste Fund	4,101,435	2,993,717	-27.0%	8,596,408	12,444,389	44.8%	47.7%	24.1%
Total Utilities	12,839,602	12,782,201	-0.4%	27,887,793	33,238,006	19.2%	46.0%	38.5%
Total All Operating Funds	47,305,435	49,815,367	5.3%	99,363,804	117,313,094	18.1%	47.6%	42.5%

Budgeted and actual expenditures exclude working capital, operating reserves, capital reserves, and interfund transfers.

General Fund Revenue

Many significant General Fund revenue sources are economically sensitive, such as sales tax and development-related fees.

- **Sales tax** revenue allocated to the General Fund for 2011 was **3.1 percent ahead** of the same period last year. A detailed analysis of total **sales tax** revenue can be found starting on page 5.
- **Utility tax** actual revenue collection was **2.0 percent ahead** of the same period last year, despite significantly lower revenue from telephone utilities (17.8 percent), which is an acceleration of recent negative trends in this category. All other utility revenue through the second quarter of 2011 exceeded revenue collections in the same period last year.
- **Other taxes** actual revenue was **5.3 percent behind** the same period last year due to lower gambling revenue.
- The **business licenses (base fee) and franchise fees** actual revenue was **11.7 percent ahead** of the same period last year. This increase is due to an increase in business license fee revenue and timing of franchise fee payments, with a late 2010 payment receipted in the first quarter of 2011. Removing this payment makes the actual revenues through the second quarter of 2011 ahead 0.5 percent compared to the same period last year.
- The **revenue generating regulatory license** fee was **17.1 percent ahead** of the same period last year and ahead of budget expectations. Part of the increase is due to business licenses in the new neighborhoods.
- The **development-related fee** revenues, were collectively **ahead 30.8 percent** compared to the same period in 2010, but fell below 2011 budget expectations. Compared to the same period last year, **building permits and plan check revenue**

were collectively **ahead 16.2 percent** and **engineering services** revenue was **44.2 percent ahead** due to receipt of two large school permits in the first quarter of 2011. **Planning fees** revenue was **ahead 73.7 percent** primarily due to two major Process IIB permits received in May, Totem Station (a mixed use project in Totem Lake) and the International Community School remodel. The increase in total development-related fees is also due to historically low collections during the same period in 2010.

Compared to the same period last year: **Grant** revenue is **ahead 229.3 percent** due to funding received for the Build America Bonds (BABs) Interest Subsidy in the second quarter of 2011; **Other intergovernmental services** revenue is **42.3 percent below** last year's actual due to the elimination of a contract to provide staffing to the regional Criminal Justice Training Center, a contract providing building inspection services to the City of Issaquah and a reduction in the provision of intergovernmental court services.

• **Internal Charges** are **8.9 percent ahead** compared to the same period last year. Most internal charges have increased due to additional costs for annexation.

- **Other financing sources** includes the transfer of FD 41 balances due to the assumption of the District, as a result of annexation. The Interfund Transfers budget is significantly lower than 2010 due to fund restructuring, including the combining of the recreation fund with the General Fund.

General Fund 2011 revenues are \$5,193,565 higher than the same period in 2010 largely due to higher property taxes budgeted in the General Fund, the receipt of grants and the timing of receipt of FD 41 revenue and despite lower other intergovernmental revenue.

The General Fund is the largest of the General Government Operating funds. It is primarily tax supported and accounts for basic services such as public safety, parks and recreation, and community development.

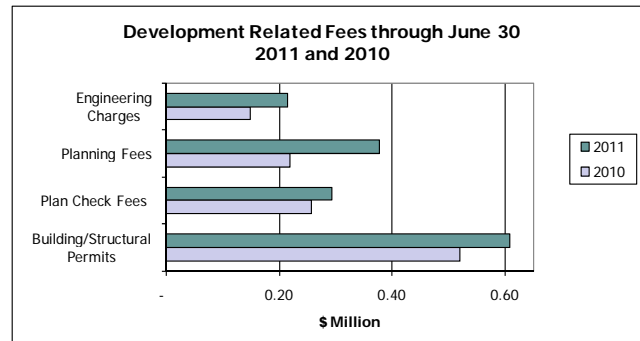
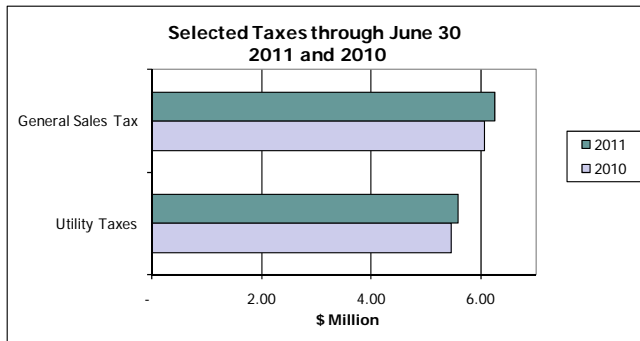
About 412 of the City's 521 regular employees are budgeted for 2011 within this fund.

General Fund Resource Category	Year-to-Date Actual			Budget			% of Budget	
	6/30/2010	6/30/2011	% Change	2010	2011	% Change	2010	2011
Taxes:								
Retail Sales Tax: General	6,070,367	6,259,322	3.1%	11,464,179	12,885,899	12.4%	53.0%	48.6%
Retail Sales Tax Credit: Annexation	-	-	N/A	-	1,129,866	N/A	N/A	N/A
Retail Sales Tax: Criminal Justice	466,365	488,643	4.8%	1,129,140	1,149,997	1.8%	41.3%	42.5%
Property Tax	5,175,037	6,906,658	33.5%	9,904,815	13,261,709	33.9%	52.2%	52.1%
Utility Taxes	5,465,327	5,576,285	2.0%	10,965,526	12,436,696	13.4%	49.8%	44.8%
Rev Generating Regulatory License	1,193,980	1,397,560	17.1%	2,567,468	2,406,234	-6.3%	46.5%	58.1%
Other Taxes	162,958	154,251	-5.3%	466,129	312,250	-33.0%	35.0%	49.4%
Total Taxes	18,534,034	20,782,719	12.1%	36,497,257	43,582,651	19.4%	50.8%	47.7%
Licenses & Permits:								
Building, Structural & Equipment Permits	519,866	608,564	17.1%	1,436,990	1,748,605	21.7%	36.2%	34.8%
Business Licenses/Franchise Fees	907,168	1,013,742	11.7%	1,720,921	2,878,614	67.3%	52.7%	35.2%
Other Licenses & Permits	119,548	140,053	17.2%	175,460	217,579	24.0%	68.1%	64.4%
Total Licenses & Permits	1,546,582	1,762,359	14.0%	3,333,371	4,844,798	45.3%	46.4%	36.4%
Intergovernmental:								
Grants and Federal Entitlements	173,032	569,756	229.3%	503,699	1,894,984	276.2%	34.4%	30.1%
State Shared Revenues & Entitlements	436,316	412,887	-5.4%	809,010	979,578	21.1%	53.9%	42.1%
Fire District #41	850,745	1,586,765	N/A	3,598,238	3,684,071	N/A	23.6%	43.1%
EMS	-	-	N/A	866,231	868,678	N/A	N/A	N/A
Other Intergovernmental Services	295,970	170,722	-42.3%	547,394	386,248	-29.4%	54.1%	44.2%
Total Intergovernmental	1,756,063	2,740,130	56.0%	6,324,572	7,813,559	23.5%	27.8%	35.1%
Charges for Services:								
Internal Charges	2,491,059	2,713,139	8.9%	4,707,822	5,589,009	18.7%	52.9%	48.5%
Engineering Services	148,488	214,056	44.2%	225,000	393,669	75.0%	66.0%	54.4%
Plan Check Fee	255,714	292,358	14.3%	408,252	1,115,779	173.3%	62.6%	26.2%
Planning Fees	217,553	377,846	73.7%	245,420	455,041	85.4%	88.6%	83.0%
Recreation	-	687,833	N/A	-	1,162,406	N/A	N/A	59.2%
Other Charges for Services	399,493	591,050	48.0%	770,890	1,709,373	121.7%	51.8%	34.6%
Total Charges for Services	3,512,307	4,876,282	38.8%	6,357,384	10,425,277	64.0%	55.2%	46.8%
Fines & Forfeits	686,442	832,510	21.3%	1,539,268	2,435,490	58.2%	44.6%	34.2%
Miscellaneous	109,870	344,863	213.9%	654,692	623,981	-4.7%	16.8%	55.3%
Total Revenues	26,145,298	31,338,863	19.9%	54,706,544	69,725,756	27.5%	47.8%	44.9%
Other Financing Sources:								
Transfer of FD 41 Balances*	-	1,724,497	N/A	-	-	N/A	N/A	N/A
Interfund Transfers	1,599,537	-	N/A	2,275,530	175,494	N/A	70.3%	N/A
Total Other Financing Sources	1,599,537	1,724,497	N/A	2,275,530	175,494	N/A	70.3%	982.7%
Total Resources	27,744,835	33,063,360	19.2%	56,982,074	69,901,250	22.7%	48.7%	47.3%

Budgeted and actual revenues exclude resources forward.

* Budget adjusted in July 2011 to reflect receipts

General Fund Revenue *continued*



General Fund Expenditures

General Fund Department Expenditures	Year-to-Date Actual			Budget			% of Budget	
	6/30/2010	6/30/2011	% Change	2010	2011	% Change	2010	2011
Non-Departmental	571,537	425,839	-25.5%	1,525,820	1,741,543	14.1%	37.5%	24.5%
City Council	226,099	195,704	-13.4%	353,130	318,241	-9.9%	64.0%	61.5%
City Manager's Office	1,437,925	1,612,473	12.1%	3,115,861	3,500,729	12.4%	46.1%	46.1%
Human Resources	514,122	587,913	14.4%	1,124,972	1,206,812	7.3%	45.7%	48.7%
City Attorney's Office	486,118	513,574	5.6%	984,121	1,160,116	17.9%	49.4%	44.3%
Parks & Community Services	3,191,200	3,063,615	-4.0%	6,722,519	7,053,447	4.9%	47.5%	43.4%
Public Works (Engineering)	1,594,898	1,625,764	1.9%	3,340,832	3,678,383	10.1%	47.7%	44.2%
Finance and Administration	1,788,892	1,944,567	8.7%	3,743,652	4,093,047	9.3%	47.8%	47.5%
Planning & Community Development	1,330,161	1,396,151	5.0%	2,730,557	3,079,987	12.8%	48.7%	45.3%
Police	8,225,550	9,417,560	14.5%	17,188,807	21,971,010	27.8%	47.9%	42.9%
Fire & Building	8,867,761	9,462,637	6.7%	17,319,527	19,664,861	13.5%	51.2%	48.1%
Total Expenditures	28,234,263	30,245,797	7.1%	58,149,798	67,468,176	16.0%	48.6%	44.8%
Other Financing Uses:								
Interfund Transfers	303,936	1,258,688	314.1%	1,024,920	3,575,316	248.8%	29.7%	35.2%
Total Other Financing Uses	303,936	1,258,688	314.1%	1,024,920	3,575,316	248.8%	29.7%	35.2%
Total Expenditures & Other Uses	28,538,199	31,504,485	10.4%	59,174,718	71,043,492	20.1%	48.2%	44.3%

Budgeted and actual expenditures exclude working capital, operating reserves, and capital reserves.

The 2011 Budget incorporates budget reductions in response to the economic downturn, additions as a result of annexation, the move to medical self-insurance, the restoration of 3.4 percent salary and benefit reductions taken in 2010, and fund restructuring to comply with accounting rule changes. These changes make comparisons to the 2010 budget challenging. Specific factors for individual departments are noted below:

Comparing to the same period last year:

- 2011 **Non-Departmental** expenditures are **25.5 percent behind** 2010 primarily due to initial savings from self-insurance for public safety retiree medical insurance premiums.
- Actual 2011 expenditures for the **City Council** are **13.4 percent behind** 2010 primarily due to a one time citizen survey paid in the first quarter of 2010.
- The **City Manager's Office** actuals are **12.1 percent ahead** due to an increase in Municipal Court staffing with corresponding workload and revenue increases and an increase in printing and professional services due to annexation.
- Actual 2011 expenditures for **Human Resources** are **14.4 percent ahead** compared to the same period in 2010 due to an increase in personnel costs related to annexation and self-insurance staffing.
- The **City Attorney's Office** expenditures are **5.6 percent ahead** compared to the same period in 2010 due to an increase in legal fees.
- Actual 2011 expenditures for the **Parks & Community Services Department** are **4.0 percent behind** 2010 due to unfilled positions and service level reductions taken in 2011.

Compared to 2010, 2011 General Fund actual expenditures are 10.4 percent ahead, despite reductions taken in response to the economic downturn, primarily due to restoration of a 3.4 percent salary reduction taken in 2010, costs associated with the recent annexation, and fund restructuring to comply with accounting rule changes.

(Continued on page 5)

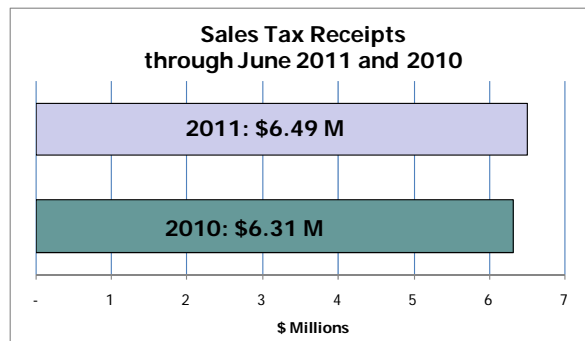
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- Actual expenditures for the **Public Works Department** are **1.9 percent ahead** of 2010 almost entirely due to staffing reallocations.
- The **Finance and Administration Department** expenditures are **8.7 percent ahead** due to election costs and one utility billing position hired to meet annexation demands related to solid waste.
- Actual 2011 expenditures for the **Planning and Community Development Department** are **5.0 percent ahead** due to personnel costs.
- Actual 2011 expenditures for the **Police Department** are **14.5 percent ahead** due to staffing (and related expenses) hired in anticipation of annexation. Increases to jail costs, which have been a concern over the last few years, have moderated due to contracts with other agencies for lower rates than those charged by King County; total charges to date are about 27 percent lower than in 2010.
- Actual 2011 expenditures for the **Fire & Building Department** are **6.7 percent ahead** due to elimination of the cost sharing implemented as IAFF's share of the 3.4 percent reduction in 2010, the replacement of portable radios and training costs. Fire suppression overtime expenses in 2011 are down about 32 percent compared to the same period last year. A summary of the funds received from the assumption of Fire District 41 on June 1 appears to the right.

Summary of Fire District 41 Funds: Revenues & Expenditures

	Capital	General Government
Revenues:		
Beginning Balance	4,000,000	1,724,497
Fire District Revenues	-	-
Total Revenues	4,000,000	1,724,497
Expenditures:		
Operating Costs (per ILA)	-	33,065
Fire District 2011 Contract	-	-
Station Consolidation Project	-	-
Total Expenditures	-	33,065
Ending Balance	4,000,000	1,691,432

Sales Tax Revenue Analysis 2011 sales tax revenue through June is **up 3.0 percent** compared to the same period last year. The primary reasons are improvements to the retail sectors (up 4.3 percent collectively over the same period last year) largely driven by auto/gas retail and general merchandise/miscellaneous retail. Declines in the contracting, other retail and wholesale sectors offset gains in other sectors in the first half of 2011. Normalizing for a one-time payment related to the State's amnesty program, the increase drops to 1.3 percent.



Review by business sectors:

- The **general merchandise/miscellaneous retail** sector is **up 6.0 percent** compared to the same period last year, despite negative performance in June.
- The **auto/gas retail** sector is **up 8.6 percent** compared to last year. This category tops the retail sector with the largest dollar increase year to date.
- The **retail eating/drinking** sector performance is **up 1.5 percent** compared to last year. While this is a small increase, it is an improvement from the consistently negative performance this sector experienced last year.
- Other retail** is **down 3.3 percent** compared to last year, despite positive performance in June.
- The **miscellaneous** sector is **up 19.5 percent** compared to last year, due to the one-time amnesty program revenue. Factoring out one-time amnesty revenues received in May and June, this category would be down 6.2 percent.
- The **communications** sector is **up 15.5 percent** compared to last year due to the significant development related activity from telecommunications companies earlier this year.
- The **services** sector is **up 1.3 percent** compared to last year, largely due to positive performance in the accommodation, internet and professional scientific categories and despite negative performance in the healthcare category. The accommodations category is up 7.7 percent or about \$8,000.
- The **contracting** sector is **down 5.8 percent** compared to last year due to various commercial tenant improvements and the completion of several large projects (e.g. Lake Washington High School and Kirkland Transit Center) that generated significant revenues last year.
- Wholesale** is **down 11.1 percent** compared to last year, largely due to continued declines in the durable goods category.

Streamlined Sales Tax

Washington State implemented new local coding sales tax rules as of July 1, 2008 as a result of joining the national Streamlined Sales Tax Agreement. Negative impacts from this change are mitigated by the State of Washington. The first two quarterly payments in 2011 total about \$56,000 and were received in March and June.

Neighboring Cities

Bellevue and Redmond 2011 sales tax revenue through June is up 5.9 percent and 60.0 percent respectively compared to the same period in 2010. Redmond is much higher due to \$4.6 million in field recoveries received in February and March. Excluding field recoveries Redmond is up 7.9 percent.

City of Kirkland Actual Sales Tax Receipts

Business Sector Group	January-June		Dollar Change	Percent Change	Percent of Total	
	2010	2011			2010	2011
Services	793,331	803,774	10,443	1.3%	12.6%	12.4%
Contracting	838,283	789,722	(48,561)	-5.8%	13.3%	12.2%
Communications	224,382	259,164	34,782	15.5%	3.6%	4.0%
Auto/Gas Retail	1,439,819	1,563,956	124,137	8.6%	22.8%	24.1%
Gen Merch/Misc Retail	868,492	920,426	51,934	6.0%	13.8%	14.2%
Retail Eating/Drinking	518,344	526,062	7,718	1.5%	8.2%	8.1%
Other Retail	820,174	793,066	(27,108)	-3.3%	13.0%	12.2%
Wholesale	402,277	357,624	(44,653)	-11.1%	6.4%	5.5%
Miscellaneous	400,243	478,415	78,172	19.5%	6.3%	7.4%
Total	6,305,345	6,492,209	186,864	3.0%	100.0%	100.0%

Kirkland's sales tax base is comprised of a variety of businesses which are grouped and analyzed by business sector (according to NAICS, or "North American Industry Classification System"). Nine business sector groupings are used to compare 2010 and 2011 year-to-date sales tax receipts in the table to the left.

City of Kirkland Actual Monthly Sales Tax Receipts

Month	Sales Tax Receipts		Dollar Change	Percent Change
	2010	2011		
January	945,992	1,082,225	136,233	14.4%
February	1,364,023	1,366,850	2,827	0.2%
March	937,460	942,887	5,427	0.6%
April	953,914	899,425	(54,489)	-5.7%
May	1,094,845	1,154,252	59,407	5.4%
June	1,009,111	1,046,570	37,459	3.7%
Total	6,305,345	6,492,209	186,864	3.0%

When analyzing monthly sales tax receipts, there are two items of special note: First, most businesses remit their sales tax collections to the Washington State Department of Revenue on a monthly basis. Small businesses only have to remit their sales tax collections either quarterly or annually, which can create anomalies when comparing the same month between two years. Second, for those businesses which remit sales tax monthly, there is a two month lag from the time that sales tax is collected to the time it is distributed to the City. For example, sales tax received by the City in June is for sales activity in April. Monthly sales tax receipts through June 2010 and 2011 are compared in the table above.

- Monthly revenue performance in 2011 has maintained the improvements seen in 2010 after the mostly double digit declines experienced throughout 2009.
- January 2011 was substantially ahead of January 2010 however, a substantial portion of the gain was one-time. Field recoveries and large one-time receipts accounted for almost half of the gain. The increase was 7.8 percent after factoring out these one-time events.
- Receipts for February reflect activity during the critical holiday retail sales month of December. Positive performance for holiday shopping experienced both nationally and regionally may have contributed to January's good results, but were not experienced in Kirkland in February.
- Receipts for April are skewed by a large field recovery received in April 2010. Excluding the field recovery would result in April 2011 being down 2.3 percent.
- 2011 sales tax revenue was budgeted to remain the same as 2010, so positive performance is a net gain to offset volatility that may be experienced later this year in this revenue source or in other revenue sources.

Kirkland's sales tax base is further broken down by business district (according to geographic area), as well as "unassigned or no district" for small businesses and businesses with no physical presence in Kirkland.

Comparing to the same period last year:

Totem Lake, which accounts for about 30 percent of the total sales tax receipts, is **up 2.1 percent** primarily due to positive performance in the automotive/gas retail sales. Almost 58

percent of this business district's revenue comes from the auto/gas retail sector.

NE 85th Street, which accounts for over 15 percent of the total sales tax receipts, is **up 2.4 percent** primarily due to automotive/gas retail sales. These sectors contribute over 39 percent of this business district's revenue.

Downtown, which accounts for over 6 percent of the total sales tax receipts, is **down 5.9 percent** due to poor performance in the retail eating/drinking sector and finance/real estate sector. The retail eating/drinking and accommodations sectors and other retail provide almost 69 percent of this business district's revenue.

Carillon Point & Yarrow Bay, which account for about 4 percent of the total sales tax receipts, are **up 60.1 percent** compared to last year primarily due to communications, other retail and the accommodations sectors, and despite poor performance in the retail eating/drinking sector. About 43 percent of this business district's revenue comes from business services, retail eating/drinking and accommodations.

Houghton & Bridle Trails, which account for about 2 percent of the total sales tax receipts, are **up 14.7 percent** collectively almost entirely due to retail food stores, primarily due to a new retail business that opened in May 2010. The retail sectors provide about 73 percent of these business districts' revenue.

Juanita, which accounts for about 2 percent of the total sales tax receipts, is **down 10.4 percent** primarily due to retail eating/drinking, retail auto/gas and business services. These sectors, along with miscellaneous retail, provide almost 73 percent of this business district's revenue.

When reviewing sales tax receipts by business district, it's important to point out that over 40 percent of the revenue received in 2011 is in the "unassigned or no district" category largely due to contracting and other revenue, which includes revenue from Internet, catalog sales and other businesses located outside of the City.

City of Kirkland Sales Tax by Business District

Business District	Jan - June Receipts		Dollar Change	Percent Change	Percent of Total	
	2010	2011			2010	2011
Totem Lake	1,915,715	1,956,895	41,180	2.1%	30.4%	30.1%
NE 85th St	972,163	995,475	23,312	2.4%	15.4%	15.3%
Downtown	436,991	411,263	(25,728)	-5.9%	6.9%	6.3%
Carillon Pt/Yarrow Bay	146,358	234,290	87,932	60.1%	2.3%	3.6%
Houghton & Bridle Trails	144,452	165,692	21,240	14.7%	2.3%	2.6%
Juanita	137,513	123,176	(14,337)	-10.4%	2.2%	1.9%
Unassigned or No District:						
Contracting	838,257	790,096	(48,161)	-5.7%	13.3%	12.2%
Other	1,713,896	1,815,322	101,426	5.9%	29.4%	29.9%
Total	6,305,345	6,492,209	186,864	3.0%	100.0%	100.0%

Sales Tax Revenue Outlook Sales tax receipts has been mostly positive for 2011 compared to 2010, as illustrated in the monthly chart on the previous page. One-time field recoveries has supplemented the increase by 1.7 percent. Upside trends pose potential risks—the general merchandise/miscellaneous retail, automotive/gas retail and miscellaneous sectors has contributed the largest amount of gain, but these sectors are very sensitive to economic conditions. Communications saw a significant increase in February, which has offset declines in all other months through June. Contracting, other retail and wholesale have not shown signs of recovery. The impact from streamlined sales tax sourcing rule changes has negatively impacted some sectors, but is offset by gains in others. The shaky economic recovery poses significant risk to the City's ability to maintain services, since sales tax is one of the primary sources of general fund revenue. Changes in revenue structure over the last few years have provided some balance to offset the volatility inherent in sales tax.

OFFICE VACANCIES:

According to CB Richard Ellis Real Estate Services, the Eastside vacancy rate is 16.0 percent for the second quarter of 2011 compared to 19.0 percent for the second quarter of 2010. Kirkland's 2011 vacancy rate is 11.5 percent, significantly lower than the 2010 rate of 28.9 percent. Continuing trends seen in 2010, the second quarter of 2011 has continued seeing a steady decrease in vacancy rates in Kirkland.

The Puget Sound regional market recovery appears to continue with 582,791 square feet of positive absorption during the second quarter, with 86 percent occurring on the Eastside. This is the fifth straight quarter of positive absorption. Positive absorption occurs when the total amount of available office space decreases during a set period.

Google and Expedia signed leases for additional space in the second quarter of 2011, which signifies continued growth.

LODGING TAX REVENUE:

Lodging tax 2011 revenue is up 6.8 percent compared to the same period last year.

Economic Environment Update Washington State's economy weakened further in June, which was highlighted as likely to be temporary, absent any low probability high impact event, according to the latest update from the Washington State Economic and Revenue Forecast Council. Employment was rising at a slow pace during the first four months; in May and June there was no growth and gains seen in aerospace and software were offset with losses in construction and the public sector. Oil prices have continued to decrease to the mid-90 dollar range per barrel after climaxing at \$113 in May. The continued decline in oil prices will put more money in consumers' pockets and may increase demand. The Japanese earthquake and tsunami have impacted the state's exports as evidenced by the decrease in The Institute for Supply Management-Western Washington Index to 56.5 from 61.1. *Note: Since the update cited above, the economy has experienced high impact events including the downgrade of the U.S. sovereign debt credit rating and a significant decline in the stock market. The national forecast is similar to what is presented for the state. The side bar on page 9 presents information on the national forecast based on a survey done by the Federal Reserve Bank of Philadelphia.*

The U.S. **consumer confidence index** fell to **58.5** in June from 61.7 in May, the lowest level in eight months. June was expected to come in around 60. Consumer confidence levels for the second quarter of 2011 have been dropping from the first quarter of 2011, which were the highest levels seen since May 2010 (63.3). This drop in consumer confidence is largely due to employment and income concerns and is a sign of a weakening economy. An index of 90 indicates a stable economy and one at or above 100 indicates growth.

King County's **unemployment rate** was **8.7 percent** in June 2011 compared to 8.9 percent in June 2010. While remaining high compared to a few years ago, King County is slightly lower than the Washington State and national rate, which is 9.3 percent.

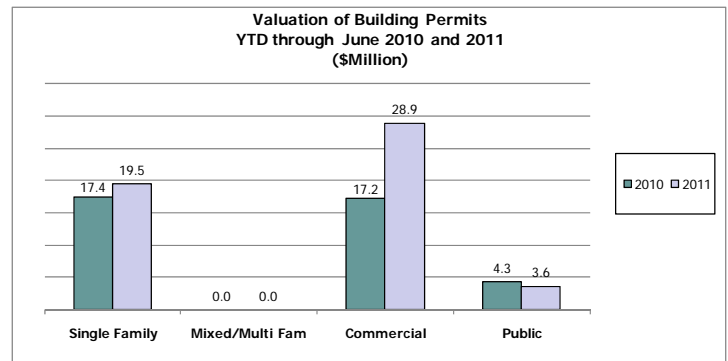
The Institute for Supply Management-**Western Washington Index** saw a decrease in June at 56.5, down from 61.1 in May. The national survey index increased to 55.3 in June from 53.5 in May. Both indices are similar to those seen throughout 2010. An index reading greater than 50 indicates a growing economy, while scores below 50 suggest a shrinking economy.

(Continued on page 8)

Local **development activity** through June comparing 2010 to 2011 as measured by the valuation of City of Kirkland building permits is illustrated in the chart to the right. Activity has improved in the single family, commercial and public sectors. However, there has been no activity in the mixed use/multifamily sectors. Through June 2011, building permit valuation was up 33.8 percent compared to June 2010. However, the second quarter 2011 building permit valuation was 7.6 percent less than the second quarter of 2010.

Closed sales of **new and existing single-family homes** on the Eastside were down 2.3 percent in June 2011 compared to June 2010. In addition, the median price of a single family home decreased 7.3 percent (\$510,000 compared to \$550,000). Closed sales for condominiums were up 10.8 percent and the median price dropped 2.1 percent (to \$235,000 from \$239,990). Countywide, closed sales were rather flat with a 0.32 percent increase compared to June 2010. Whereas, the countywide median home price fell almost ten percent year-over-year.

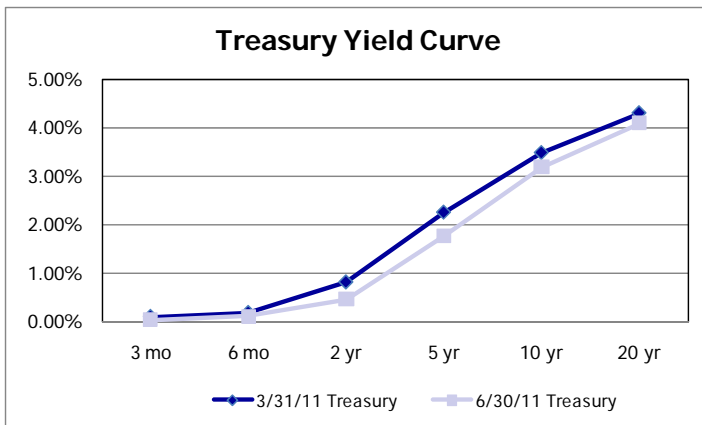
Seattle metro consumer price index (CPI) in June was the highest it has been since December 2009, at 3.7 percent. The Seattle index is calculated bi-monthly. The national index was 4.1 percent in May and June. Since December, the CPI in Seattle and nationally has increased by more than 2.5 percent. This increase was impacted largely by higher prices for energy, including gasoline. The June index is typically the contractual basis for cost of living (COLA) increases. Employees received no cost of living adjustment in 2010 or 2011, due to negative CPI's. The City has five of six bargaining agreements ending December 31, 2011. CPI is used to identify periods of inflation or deflation.



Investment Report

MARKET OVERVIEW

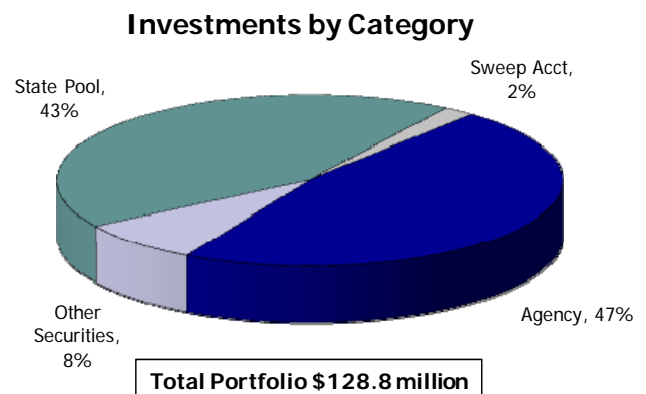
The Fed Funds rate remained at 0.25 percent for the first half of 2011 and is not expected to change until the 2nd quarter of 2012. The economy continues to struggle with only moderate improvement. For the 2nd quarter of 2011 the yield curve dropped slightly along every point of the curve.



CITY PORTFOLIO

The primary objectives for the City of Kirkland's investment activities are: legality, safety, liquidity and yield. Additionally, the City diversifies its investments according to established maximum allowable exposure limits so that reliance on any one issuer will not place an undue financial burden on the City.

The City's portfolio increased in the 2nd quarter of 2011 to \$128.8 million compared to \$116.4 million on March 31, 2011. The increase in the portfolio is related to the normal cash flows of the 2nd quarter, as the first half of property taxes is received at the end of April and early May and the Fire District 41 funds transferred to the City.



Diversification

The City's current investment portfolio is composed of Government Sponsored Enterprises (GSEs) bonds, State and Local Government bonds, the State Investment Pool and an overnight bank sweep account. City investment procedures allow for 100% of the portfolio to be invested in U.S. Treasury or Federal Government obligations.

2011 ECONOMIC OUTLOOK and INVESTMENT STRATEGY

The outlook for growth in the U.S. economy now looks slower than it did just three months ago, according to 44 forecasters surveyed by the Federal Reserve Bank of Philadelphia. The U.S. economy is expected to grow at an annual rate of 2.7 percent in 2011. CPI inflation expectations have increased to average 3.1 percent in 2011 and 2.2 percent in 2012. The unemployment rate is expected to average 8.7 percent in 2011 and fall to 8.1 percent in 2012. The Fed Funds rate, currently at 0.25%, is expected to remain at this level throughout 2011.

The duration of the portfolio will decrease as securities mature and are called. Opportunities for increasing portfolio returns are scarce as shorter term interest rates continue at historically low levels. New security purchases will be made as opportunities to obtain moderate returns become available. During periods of low interest rates the portfolio duration should be shorter with greater liquidity so that the City is in a position to be able to purchase securities with higher returns when interest rates begin to rise. The State Pool is currently at 0.16% and will continue to remain low as the Fed Funds rate remains at 0.00 to 0.25 percent. Total estimated investment income for 2011 is \$785,000.

Investment Report *continued*

Liquidity

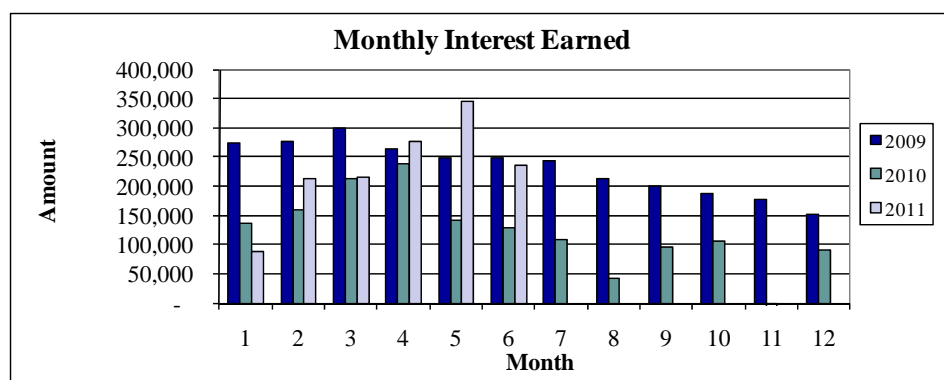
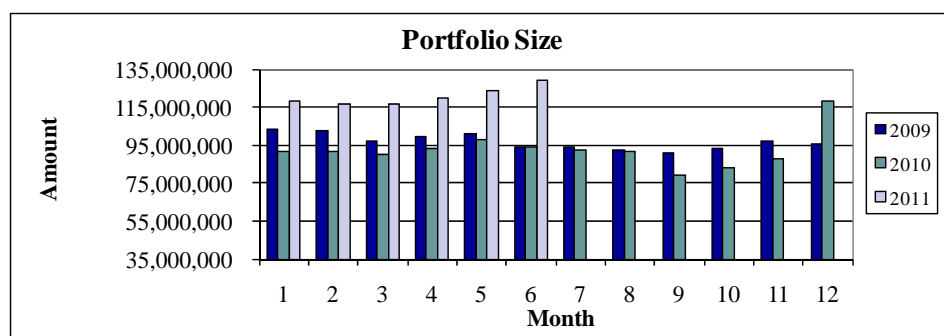
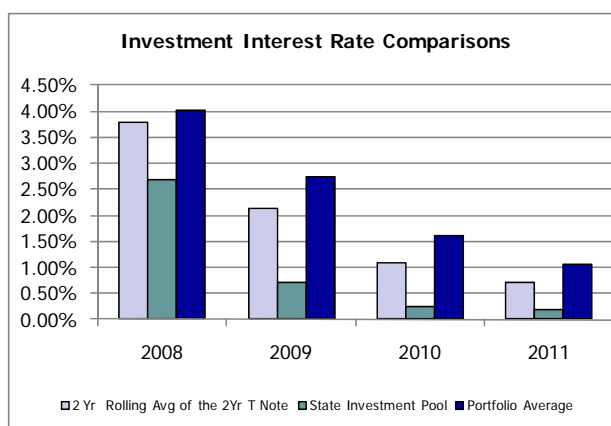
The City of Kirkland Investment Policy, Section 13, states that the maximum weighted average maturity (WAM) of the total portfolio shall not exceed 3 years. This maximum is established to limit the portfolio to excessive market exposure. The average maturity of the City's investment portfolio increased from 1.28 years on

March 31, 2011 to 1.81 years on June 30, 2011 due to the purchase of longer term securities which gained slightly higher yields. It is expected that those securities will be called on their call dates as the interest rates of the securities are higher than current rates.

Benchmark Comparison	March 31, 2011	June 30, 2011
City Yield to Maturity (YTM)	1.03%	1.21%
City Average YTM	1.08%	1.06%
City Year to Date Cash Yield	1.22%	0.97%
90 Day Treasury Bill	0.09%	0.03%
2 yr Rolling Avg 2 yr T Note	0.78%	0.72%

Yield

The City Portfolio yield to maturity increased from 1.03 percent on March 31, 2011 to 1.21 percent on June 30, 2011. The City's portfolio benchmark is the range between the 90 day Treasury Bill and the 2 year rolling average of the 2 year Treasury Note. This benchmark is used as it is reflective of the maturity guidelines required in the Investment Policy adopted by City Council. The City's portfolio outperformed both the 90 day T Bill and the 2 year rolling average of the 2 year Treasury Note, which was 0.72 percent on June 30, 2011. The City's practice of investing further out on the yield curve than the State Investment Pool results in earnings higher than the State Pool during declining interest rates and lower earnings than the State Pool during periods of rising interest rates. This can be seen in the graph above.



Reserves are an important indicator of the City's fiscal health and effectively represent "savings accounts" that are established to meet unforeseen budgetary needs (general purpose reserves) or are dedicated to a specific purpose. The reserves are listed with their revised estimated balances at the end of the biennium as of June 30, 2011.

Reserve Analysis

General Purpose Reserves

- The **Revenue Stabilization Reserve** was used almost in its entirety during the 2009-10 biennium as part of the budget balancing strategy to address the severe economic downturn and allowed the City to mitigate some negative impacts to services. General Fund 2010 year-end cash was used to replenish this reserve in the amount of \$600,000 in 2011 and further replenishment will be a high priority.
- The **Building and Property Reserve** is a planned use as part of the funding sources available for facility expansion and renovation projects, which include the new Public Safety Building, Maintenance Center, and City Hall.

General Capital Reserves

- The downturn in real estate transactions over the last few years has significantly impacted **Real Estate Excise Tax (REET)** collections resulting in adjustments to capital project planning to reflect available funding. Revenue is 16.9 percent ahead of the same period last year and appears to be on track to well exceed budget. However, it also is about half of the revenue received in 2007.
- **Impact fees** have also been significantly reduced as a result of the severe downturn in development activity, resulting in adjustments to capital projects plans. 2011 revenue is 56 percent ahead of the same period in 2010 largely due to an improvement in transportation fees. Even still, transportation fees are only at 11 percent of the budget at midyear. There is no planned use for projects in the current budget cycle since these revenue sources are expected to remain extremely low compared to historical trends and most likely will remain there until development activity improves.

Internal Service Fund Reserves

- **Systems Reserve** (Information Technology) during the current biennium is expected to use most of this reserve for replacement of the Maintenance Management System.
- The **Radio Reserve** (Fleet) was used in its entirety as a small part of the funding source for a major replacement of police and fire radios that began in 2010, and is expected to finish by the end of 2012.
- City Council provided direction to staff as part of the 2011-12 budget process to develop recommendations for establishing new sinking fund reserves for technology and public safety equipment (including radios) for consideration in the 2013-14 budget process to address the lack of ongoing funding for the periodic replacement of these items.

General Government & Utility Reserves Targets Summary

Reserves	2011 Beginning Balance	Adopted 2012 Ending Balance	Revised 2012 Ending Balance	2011-12 Target	Revised Over (Under) Target
GENERAL PURPOSE RESERVES WITH TARGETS					
General Fund Reserves:					
General Fund Contingency	50,000	50,000	50,000	50,000	0
General Oper. Reserve (Rainy Day)	2,806,513	2,806,513	2,806,513	4,127,496	(1,320,983)
Revenue Stabilization Reserve	131,431	731,431	731,431	2,279,251	(1,547,820)
Council Special Projects Reserve	201,534	251,534	233,534	250,000	(16,466)
Contingency	2,051,870	2,201,870	2,201,870	4,016,232	(1,814,362)
General Capital Contingency:	4,844,957	4,669,463	4,669,463	6,766,320	(2,096,857)
General Purpose Reserves with Targets	10,086,305	10,710,811	10,692,811	17,489,299	(6,796,488)
ALL OTHER RESERVES WITH TARGETS					
General Fund Reserves:					
Litigation Reserve	70,000	70,000	70,000	50,000	20,000
Firefighter's Pension Reserve	1,595,017	1,734,215	1,734,215	1,568,207	166,008
Health Benefits Fund:					
Claims Reserve	0	1,424,472	1,424,472	1,424,472	0
Rate Stabilization Reserve	0	500,000	500,000	500,000	0
Excise Tax Capital Improvement:					
REET 1	1,530,280	1,019,907	1,019,907	1,035,000	(15,093)
REET 2	7,121,695	4,975,718	4,892,465	11,484,000	(6,591,535)
Water/Sewer Operating Reserve:	1,979,380	1,979,380	1,939,380	1,979,380	(40,000)
Water/Sewer Debt Service Reserve:	822,274	508,717	508,717	508,717	0
Water/Sewer Capital Contingency:	1,793,630	1,793,630	1,793,630	250,000	1,543,630
Surface Water Operating Reserve:	412,875	412,875	412,875	412,875	0
Surface Water Capital Contingency:	858,400	858,400	858,400	758,400	100,000
Other Reserves with Targets	16,183,551	15,277,314	15,154,061	19,971,051	(4,816,990)
Reserves without Targets	30,665,367	36,312,121	36,192,121	n/a	n/a
Total Reserves	56,935,223	62,300,246	62,038,993	n/a	n/a

The target comparison reflects revised ending balances to the targets established in the budget process for those reserves with targets

General Purpose reserves are funded from general revenue and may be used for any general government function.

All Other Reserves with Targets have restrictions for use either from the funding source or by Council-directed policy (such as the Litigation Reserve).

The summary to the right details all Council authorized uses and additions through the second quarter of 2011.

USES AND ADDITIONS HIGHLIGHTS

RESERVE	AMOUNT	DESCRIPTION
2011 Council Authorized Uses		
2011 First Quarter Total Uses	\$248,253	
Council Special Projects Reserve	\$3,000	CDBG Consortium Agreement
	\$10,000	Green Kirkland Staffing

2011 Council Authorized Additions

No Authorized City Council additions as of June 30, 2011

General Fund and Contingency reserves are funded from general purpose revenue and are governed by Council-adopted policies.

Note: Fund structure changes required by new accounting standards moved many of the General Purpose reserves out of the Parks & Municipal Reserve Fund (which was closed) and to the General Fund.

Special Purpose reserves reflect both restricted and dedicated revenue for specific purpose, as well as general revenue set aside for specific purposes.

General Capital Reserves provide the City the ability to respond to unexpected changes in costs and accumulate funds for future projects. It is funded from both general revenue and restricted revenue.

Utility reserves are funded from utility rates and provide the utilities with the ability to respond to unexpected costs and accumulate funds for future replacement projects.

Internal service funds are funded by charges to operating departments. They provide for the accumulation of funds for replacement of equipment, as well as the ability to respond to unexpected costs.

Reserves	Description	2011 Beginning Balance	Adopted 2012 Ending Balance	Additional Authorized Uses/Additions	Revised 2012 Ending Balance
GENERAL FUND/CONTINGENCY					
General Fund Reserves:					
General Fund Contingency	Unexpected General Fund expenditures	50,000	50,000	0	50,000
General Oper. Reserve (Rainy Day)	Unforeseen revenues/temporary events	2,806,513	2,806,513	0	2,806,513
Revenue Stabilization Reserve	Temporary revenue shortfalls	131,431	731,431	0	731,431
Building & Property Reserve	Property-related transactions	1,972,213	1,972,213	0	1,972,213
Council Special Projects Reserve	One-time special projects	201,534	251,534	(18,000)	233,534
Contingency	Unforeseen expenditures	2,051,870	2,201,870	0	2,201,870
Total General Fund/Contingency		7,213,561	8,013,561	(18,000)	7,995,561
SPECIAL PURPOSE RESERVES					
General Fund Reserves:					
Litigation Reserve	Outside counsel costs contingency	70,000	70,000	0	70,000
Labor Relations Reserve	Labor negotiation costs contingency	70,606	70,606	0	70,606
Police Equipment Reserve	Equipment funded from seized property	50,086	50,086	0	50,086
LEOFF 1 Police Reserve	Police long-term care benefits	618,079	618,079	0	618,079
Facilities Expansion Reserve	Special facilities expansions reserve	800,000	800,000	0	800,000
Development Services Reserve	Revenue and staffing stabilization	502,011	652,011	0	652,011
Tour Dock	Dock repairs	81,745	81,745	0	81,745
Tree Ordinance	Replacement trees program	29,117	29,117	0	29,117
Donation Accounts	Donations for specific purposes	185,026	185,026	0	185,026
Revolving Accounts	Fee/reimbursement for specific purposes	436,386	436,386	0	436,386
Lodging Tax Fund	Tourism program and facilities	146,384	123,566	(15,000)	108,566
Cemetery Improvement	Cemetery improvements/debt service	439,415	439,415	0	439,415
Off-Street Parking	Downtown parking improvements	10,776	10,776	0	10,776
Firefighter's Pension	Long-term care/pension benefits	1,595,017	1,734,215	0	1,734,215
Total Special Purpose Reserves		5,034,648	5,301,028	(15,000)	5,286,028
GENERAL CAPITAL RESERVES					
Excise Tax Capital Improvement:					
REET 1	Parks/transportation/facilities projects, parks debt service	1,530,280	1,019,907	0	1,019,907
REET 2	Transportation capital projects	7,121,695	4,975,718	(83,253)	4,892,465
Impact Fees					
Roads	Transportation capacity projects	525,095	1,112,245	0	1,112,245
Parks	Parks capacity projects	2,033	3,038	0	3,038
Street Improvement	Street improvements	1,092,258	1,092,258	(5,000)	1,087,258
General Capital Contingency	Changes to General capital projects	4,844,957	4,669,463	0	4,669,463
Total General Capital Reserves		15,116,318	12,872,629	(88,253)	12,784,376
UTILITY RESERVES					
Water/Sewer Utility:					
Water/Sewer Operating Reserve	Operating contingency	1,979,380	1,979,380	(40,000)	1,939,380
Water/Sewer Debt Service Reserve	Debt service reserve	822,274	508,717	0	508,717
Water/Sewer Capital Contingency	Changes to Water/Sewer capital projects	1,793,630	1,793,630	0	1,793,630
Water/Sewer Construction Reserve	Replacement/re-prioritized/new projects	7,870,665	9,871,542	(100,000)	9,771,542
Surface Water Utility:					
Surface Water Operating Reserve	Operating contingency	412,875	412,875	0	412,875
Surface Water Capital Contingency	Changes to Surface Water capital	858,400	858,400	0	858,400
Surface Water-Transp. Related Rsv	Replacement/re-prioritized/new projects	2,483,250	3,666,250	0	3,666,250
Surface Water Construction Reserve	Trans. related surface water projects	2,848,125	3,376,431	0	3,376,431
Total Utility Reserves		19,068,599	22,467,225	(140,000)	22,327,225
INTERNAL SERVICE FUND RESERVES					
Health Benefits:					
Claims Reserve	Health benefits self insurance claims	0	1,424,472	0	1,424,472
Rate Stabilization Reserve	Rate stabilization	0	500,000	0	500,000
Equipment Rental:					
Vehicle Reserve	Vehicle replacements	7,718,221	8,047,063	0	8,047,063
Radio Reserve	Radio replacements	0	0	0	0
Information Technology:					
PC Replacement Reserve	PC equipment replacements	258,311	318,646	0	318,646
Technology Initiative Reserve	Technology projects	690,207	690,207	0	690,207
Major Systems Replacement Reserve	Major technology systems replacement	245,500	84,900	0	84,900
Facilities Maintenance:					
Operating Reserve	Unforeseen operating costs	550,000	550,000	0	550,000
Facilities Sinking Fund	20-year facility life cycle costs	1,039,858	2,030,515	0	2,030,515
Total Internal Service Fund Reserves		10,502,097	11,721,331	0	11,721,331
Grand Total		56,935,223	62,300,246	(261,253)	62,038,993



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The Financial Management Report (FMR) is a high-level status report on the City's financial condition that is produced quarterly.

- It provides a **summary budget to actual comparison** for year-to-date revenues and expenditures for all operating funds. The report also compares this year's actual revenue and expenditure performance to the prior year.
- The **Sales Tax Revenue Analysis** report takes a closer look at the City's largest and most economically sensitive revenue source.
- **Economic environment** information provides a brief outlook at the key economic indicators for the Eastside and Kirkland such as office vacancies, residential housing prices/sales, development activity, inflation and unemployment.
- The **Investment Summary** report includes a brief market overview, a snapshot of the City's investment portfolio, and the City's year-to-date investment performance.
- The **Reserve Summary** report highlights the uses of and additions to the City's reserves in the current year as well as the projected ending reserve balance relative to each reserve's target amount.

Economic Environment Update References:

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- Washington State Employment Security Department
- Washington State Department of Revenue
- Washington State Department of Labor & Industries
- City of Kirkland Building Division
- City of Kirkland Finance & Administration Department